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STANCOR LIMITED

Whitby, Ontario · Canada · 416/668-3315

July 8, 1968

TO THE SHAREHOLDERS:

As you know, the Company suffered a severe setback in 1967. During the first half of the year, the Peppler Division reported an operating loss of approximately one half million dollars. This loss resulted from serious problems in all phases of the Peppler operation. A new product line, which had been developed for sale in the mass market, proved to be unsaleable in any market, except at distressed prices. Much of the productive capacity had been occupied by this product line for several months. Expanded production facilities and associated overhead costs were much too large for the level of sales that could be sustained. In addition, substantial production inefficiencies were created for some time, by the extent of the changes made in products and production facilities.

Because of a soft market for home furnishings during much of 1967, the Sklar and Peppler-Selig Divisions managed only to break even on operations in the first half. It was, therefore, impossible for the Company to absorb the Peppler loss. By May of 1967, the ability of the Company to pay its trade suppliers had deteriorated badly, and the bank had refused to increase its line of credit. It was obvious that drastic action had to be taken if the Company was to be saved.

Approximately mid-year, the senior management of the Company was replaced and a program of recovery was undertaken. Major changes were made in the Peppler product line. Within a period of two to three months, labour costs at Hanover were cut by approximately 25%. The Peppler sales force was expanded and improved, using the well-established Sklar sales organization as a base. Overhead costs were slashed at both the Sklar and Peppler Divisions. The Peppler-Selig Division was sold to obtain urgently needed cash, and to allow senior management to concentrate its efforts more strongly on the larger Divisions.

The corrective action taken at the Peppler Division produced immediate reductions in operating losses. By the end of the year, Peppler had recovered to the point that it was operating currently at approximately a break-even level. The Sklar Division completed the year with an operating profit. Overall, the operating loss, before interest charges, was reduced to $71,790 for the second half of the year, as compared with a loss of $548,216 in the first half.

The success of the recovery program has been so marked that the Company should be well into profitable operations in 1968, given normal market conditions. This is confirmed by operating results to date. With the existing financial condition of the Company, however, it will be impossible to service the long term debt. At December 31, 1967, the Company was in arrears on

Continued.......

long term debt to the extent of approximately $260,000. In 1968, further payments on long term debt of approximately $485,000 become due, in addition to bank interest of approximately $200,000.

To resolve the current problem of debt arrears, and to put the Company in a position to carry its long term debt in the future, management has developed a plan for financial reconstruction. Agreement on the plan has been reached with the Bondholders and the General Mortgage Debentureholders, the two senior groups of security holders. This agreement, however, is conditional on acceptance of the plan by the Shareholders, the Warrantholders, and the Collateral Trust Debentureholders as well.

Enclosed, in addition to the Company's Annual Report for 1967,is a copy of the Plan of Reorganization approved by the Board of Directors June 28, 1968, together with the other relevant documents. Your management is confident that with the approved reorganized financial structure, Stancor Limited can be made the success it was originally expected to be.

Yours very truly,

STANCOR LIMITED,

Samuel Sklar

Samuel Sklar,
President.

File

STANCOR LIMITED

CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1967

STANCOR LIMITED
(Incorporated under the laws of Ontario)
and subsidiary companies

CONSOLIDATED BALANCE SHEET

DECEMBER 31, 1967
(with comparative figures as at December 31, 1966)

ASSETS

	1967	1966
CURRENT ASSETS:		
Cash		$ 37,102
Accounts receivable	$2,239,829	2,858,569
Inventories (note 3)	2,023,692	2,199,520
Prepaid expenses and other current assets	37,220	91,259
Total current assets	4,300,741	5,186,450
PROPERTY, PLANT AND EQUIPMENT (note 4)	3,397,774	3,632,337
DEFERRED CHARGES (note 5):		
Deferred start-up and reorganization costs		275,000
Share issue expenses		141,595
Other deferred charges		33,082
		449,677
GOODWILL - at cost	2,805,727	2,805,727
	$10,504,242	$12,074,191

LIABILITIES

	1967	1966
CURRENT LIABILITIES:		
Bank indebtedness (note 6)	$2,766,452	$2,520,215
Accounts payable and accrued charges	1,255,421	1,389,312
Sales and other taxes payable	154,402	214,437
Long-term debt principal and interest payments due but unpaid (note 1)	260,267	
Long-term debt principal due within one year (note 7)	177,000	132,000
Total current liabilities	4,613,542	4,255,964
NON-CURRENT LIABILITIES:		
Long-term debt (note 7)	3,928,295	4,211,344
Less unamortized debt discount and expense	194,428	209,492
	3,733,867	4,001,852
SHAREHOLDERS' EQUITY:		
Capital stock (note 8)	3,713,800	3,713,800
Contributed surplus	8,500	8,500
(Deficit) earned surplus (note 7)	(1,565,467)	94,075
	2,156,833	3,816,375
	$10,504,242	$12,074,191

On behalf of the Board:

D.R. Annett Director

Samuel Sklar Director

See accompanying notes to consolidated financial statements.

STANCOR LIMITED
and subsidiary companies

CONSOLIDATED STATEMENT OF DEFICIT

FOR THE YEAR ENDED DECEMBER 31, 1967
(with comparative figures for 1966)

	1967	1966
EARNED SURPLUS, BEGINNING OF YEAR	$ 94,075	$ 18,310
Net (loss) profit for the year	(1,165,509)	108,559
Loss on sale of assets of Peppler-Selig Limited, a subsidiary company (note 2)	(44,356)	
Write-off of deferred charges (note 5):		
Deferred start-up and reorganization costs	(275,000)	
Share issue expenses	(141,595)	
Other deferred charges	(33,082)	
Dividend on preference shares		(32,794)
(DEFICIT) EARNED SURPLUS, END OF YEAR	$(1,565,467)	$ 94,075

See accompanying notes to consolidated financial statements.

STANCOR LIMITED
and subsidiary companies

CONSOLIDATED STATEMENT OF PROFIT AND LOSS

FOR THE YEAR ENDED DECEMBER 31, 1967
(with comparative figures for 1966)

	1967	1966
NET SALES	$12,043,017	$10,234,612
OPERATING COSTS AND EXPENSES:		
Cost of goods sold	10,180,532	8,135,583
Marketing expenses	1,223,144	899,043
General and administrative expenses	964,194	648,157
Depreciation	295,153	199,367
	12,663,023	9,882,150
OPERATING (LOSS) PROFIT BEFORE INTEREST	(620,006)	352,462
INTEREST:		
Interest on bank indebtedness	220,346	113,338
Interest on long-term debt	325,157	130,565
	545,503	243,903
NET (LOSS) PROFIT FOR THE YEAR	$(1,165,509)	$ 108,559

See accompanying notes to consolidated financial statements.

STANCOR LIMITED
and subsidiary companies

CONSOLIDATED STATEMENT OF SOURCE AND APPLICATION OF FUNDS

FOR THE YEAR ENDED DECEMBER 31, 1967
(with comparative figures for 1966)

	1967	1966
SOURCE OF FUNDS:		
Sale of property, plant and equipment, less proceeds of sale of the fixed assets of Peppler-Selig Limited held by the trustee for the first mortgage bondholders (note 7)	$ 9,524	
Proceeds from issues of bonds, debentures, notes and shares, net of issue expenses		$5,318,926
Working capital of business acquired, at date of acquisition		611,425
Total	9,524	5,930,351
APPLICATION OF FUNDS:		
Operations -		
Net loss (profit) for the year	1,165,509	(108,559)
Loss on sale of assets of Peppler-Selig Limited, a subsidiary company, charged to deficit account (note 2)	44,356	
(Deduct) or add non-cash charges:		
Depreciation	(295,153)	199,367
Amortization of debt discount and expense	(15,064)	12,536
Funds applied to (provided from) operations	899,648	(320,462)
Additions to property, plant and equipment	176,163	1,239,826
Provision for long-term debt due within one year (note 7)	177,000	132,000
Acquisition of Sklar Furniture Company		4,000,000
Deferred start-up and reorganization costs		275,000
Dividend on preference shares		32,794
Other deferred charges		20,583
Total	1,252,811	5,379,741
DECREASE (INCREASE) IN WORKING CAPITAL	1,243,287	(550,610)
WORKING CAPITAL, BEGINNING OF YEAR	930,486	379,876
WORKING CAPITAL (DEFICIENCY), END OF YEAR (note 1)	$ (312,801)	$ 930,486

See accompanying notes to consolidated financial statements.

STANCOR LIMITED
and subsidiary companies

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 1967

1. Proposed plan of reconstruction

Because of the operating loss incurred in 1967 and the consequent reduction in working capital, the company is in default of certain provisions of the trust deeds relating to the outstanding bonds and debentures. The specific defaults are as follows:

(i) Interest and principal payments on the bonds and debentures are in arrears in the amount of $260,267, as follows:

Interest	$153,267
Principal	107,000
	$260,267

(ii) Consolidated working capital has fallen below the required minimum levels set out in the provisions relating to the first mortgage bonds ($500,000 up to June 30, 1967, $750,000 from July 1, 1967 to December 31, 1967, $1,000,000 from January 1, 1968 to December 31, 1968, and $1,500,000 thereafter).

Management has been developing a plan of financial reconstruction in co-operation with representatives of the bondholders, the debenture holders and the shareholders. The objectives of the plan are to relieve the company of its present position in default, and to reduce the fixed burden of interest and sinking fund payments in the future. Substantial progress has been made to date and agreement in principle on most issues has been achieved with the larger bond and debenture holders. A formal proposal is expected to be ready for ratification by security holders early in 1968.

2. Principles of consolidation

The accounts of all subsidiary companies have been included in the consolidation. Effective August 11, 1967, the company sold substantially all the assets and business of Peppler-Selig Limited, one of its subsidiary companies. The loss on the sale of the assets amounting to $44,356 has been charged to deficit account. The consolidated statement of profit and loss includes the earnings of that business for the period up to August 11, 1967.

3. Inventories

Inventories are valued at the lower of cost or net realizable value and consist of the following:

	1967	1966
Raw materials	$1,146,298	$1,074,208
Work in process	310,518	518,807
Finished goods	566,876	606,505
	$2,023,692	$2,199,520

4. Property, plant and equipment

	Cost	Accumulated depreciation	Net investment 1967	Net investment 1966
Land	$ 61,398		$ 61,398	$ 69,920
Buildings	1,880,575	$ 209,993	1,670,582	1,793,327
Leasehold improvements	207,619	29,129	178,490	102,004
Machinery and equipment	2,737,508	1,250,204	1,487,304	1,667,086
	$4,887,100	$1,489,326	$3,397,774	$3,632,337

5. Write-off of deferred charges

In 1966 the company treated as "deferred start-up and reorganization costs" certain costs amounting to $275,000 attributable to the start-up phase of the company's new manufacturing facilities in Hanover. At that time it was the intention that these deferred costs would be

charged to operations over the three year period 1967 to 1969 inclusive. In 1967 the company's management decided to write off the entire amount of these costs, together with deferred share issue expenses of $141,595 and certain other deferred charges of $33,082, rather than to amortize such costs over a period of years. These write-offs are shown as charges against deficit account in 1967.

6. Bank indebtedness

Bank indebtedness is secured by a pledge of the accounts receivable and inventories. In addition, two subsidiary companies have each issued to the bank as collateral security, floating charge debentures in the amount of $1,000,000 on all their assets, such debentures being subordinate to the first floating charge created by the first mortgage bonds, as referred to in note 7.

7. Long-term debt

	1967	1966
First mortgage sinking fund bonds due September 15, 1986 -		
$7\frac{1}{2}\%$ series A, payable in Canadian dollars	$1,600,000	$1,600,000
7% series B, payable in United States dollars (U.S. $500,000)	537,969	537,969
Convertible subordinate general mortgage debentures due September 15, 1978 -		
$7\frac{1}{2}\%$ series A, payable in Canadian dollars	500,000	500,000
7% series B, payable in United States dollars (U.S. $400,000)	430,375	430,375
$6\frac{1}{2}\%$ convertible collateral trust debentures due November 15, 1977	1,250,000	1,250,000
6% notes payable		25,000
	4,318,344	4,343,344
Less:		
Instalments due within one year, included in current liabilities	177,000	132,000
Instalments in arrears, included in current liabilities	107,000	
Portion of the proceeds of sale (plus interest) of the assets of Peppler-Selig Limited held by the trustee for the first mortgage bondholders	106,049	
	390,049	132,000
	$3,928,295	$4,211,344

The main provisions relating to the long-term debt are as follows:

(a) Sinking funds -

Sinking fund instalments required up to December 31, 1972 for the retirement of bonds and debentures are as follows:

1967 (in arrears)	$107,000
1968 to 1971	177,000 per year
1972	306,000

(b) Security -

The first mortgage bonds are secured by a first mortgage on substantially all the fixed assets, together with a first floating charge on all other assets, subject to the pledge of accounts receivable and inventories as security for bank indebtedness as referred to in note 6.

The convertible subordinate general mortgage debentures are secured by a second mortgage on the fixed assets, together with a floating charge on all other assets, subordinate to the floating charge security for bank indebtedness, as referred to in note 6.

The convertible collateral trust debentures are secured by a pledge of the shares of the subsidiary companies.

(c) Redemption -

The bonds and debentures are redeemable in whole or in part at the company's option (subject to the payment of specified premiums on a declining scale) as follows:

In the case of the first mortgage bonds and the general mortgage debentures - after September 15, 1971.

In the case of the collateral trust debentures - after November 15, 1968.

(d) Convertibility into common shares -

The general mortgage debentures are convertible at the holder's option into common shares without par value at a price of $8.00 per share in the period to September 14, 1972 and $10.00 per share in the period September 15, 1972 to September 14, 1978.

The collateral trust debentures are convertible at the holder's option into common shares without par value at a price of $8.00 per share in the period to November 14, 1972 and $10.00 per share in the period November 15, 1972 to November 14, 1978.

(e) Restrictions re dividends, redemption of preference shares, working capital, etc. -

The trust deed relating to the first mortgage bonds contains certain restrictions on the payment of dividends on both preference and common shares and on the redemption of preference shares, and provides for the maintenance of working capital in certain minimum amounts. As a result of these restrictive covenants, dividends paid after January 1, 1966 on preference and common shares may not in total exceed 75% of consolidated net income earned after January 1, 1966. In addition, preference share dividends may not reduce consolidated current assets below 150% of consolidated current liabilities, and total shareholders' equity below $3,500,000. For common share dividends and redemptions of preference shares, the respective minimums are 200% and $4,000,000.

8. Capital stock

Authorized:

225,000 first preference shares with a par value of $10 each, issuable in series, of which 200,000 shares are designated as 6% cumulative redeemable convertible first preference shares 1966 series, redeemable at $10.60 after March 1, 1969

1,000,000 common shares without par value

Issued:

200,000 first preference shares	$2,000,000
333,500 common shares	1,713,800
	$3,713,800

(a) Convertibility of preference shares -

The preference shares are convertible at the holder's option into common shares on the basis of $1\frac{1}{4}$ common shares for each preference share during the period to March 1, 1973, and 1 common share for each preference share during the period March 2, 1973 to March 1, 1978.

(b) Arrears of dividends on preference shares -

As at December 31, 1967, the cumulative dividends on the outstanding preference shares were in arrears in the amount of $120,000 for the period August 1, 1966 to July 31, 1967.

(c) Restrictions re dividends on common shares -

The terms of issue of the preference shares provide certain restrictions on the payment of dividends on common shares. These restrictions, however, are less restrictive than those imposed by the trust deed for the first mortgage bonds to which reference was made in note 7.

(d) Reservation of common shares -

577,750 common shares are reserved as follows:

	Number of shares
(i) For possible issue upon the exercise of the 298,200 share purchase warrants presently outstanding. Such warrants entitle the holders thereof to purchase common shares at a price of $8.00 per share until June 15, 1975, subject to adjustment under certain conditions.	298,200 shares
(ii) For possible issue upon the exercise of stock options granted to officers or employees of the company and its subsidiaries. These options entitle the holders thereof to purchase shares at a price of $8.00 per share exercisable for periods up to five years. As of December 31, 1967, none of the options had been exercised.	7,000
(iii) For possible issue on conversion of the general mortgage and collateral trust debentures referred to in note 7 above.	272,550
	577,750 shares

Note: To the extent that preference shares are converted into common shares, the Corporations Act of Ontario provides that the number of common shares authorized and issued will be increased accordingly.

9. Tax loss carry forward

As at December 31, 1967, the company and its subsidiaries have losses available for carry forward as deductions against future years' profits as well as unclaimed capital cost allowances in excess of depreciation written. At current tax rates, the tax credits which would result from the carry forward of these amounts will, if realized, amount to approximately $725,000.

10. Pension plans

Certain salaried employees participate in a contributory pension plan which was introduced on January 1, 1966. Hourly-paid employees in the company's plants at Hanover are covered by a non-contributory joint industry-union pension plan. The total pension cost charged to income (including amounts paid to government pension plans) was $146,132 in 1967 and $122,116 in 1966.

The unfunded past service liability under the salaried plan is $22,000, which is being funded over 14 years.

11. Long-term leases

The company's Whitby plant is held under a long-term lease expiring in 1986, with renewal options for two further five year periods. The fixed annual rental on this property (exclusive of taxes, insurance and maintenance costs) amounts to $114,000 during the primary term of the lease and will decrease by one-third if the renewal options are exercised.

The Toronto and Montreal showrooms are held under leases at fixed annual rentals (exclusive of taxes, insurance and maintenance costs) as follows:

1968 and 1969	$10,000
1970 to 1975	79,000
1976	76,000
1977	23,000

12. Remuneration of directors and officers

The total remuneration paid or payable by the company to its directors and senior officers amounted to $187,580 in 1967. This includes the salaries of five full-time executives and three former officers, as well as termination payments to two of those officers.

AUDITORS' REPORT

To the Shareholders of Stancor Limited:

We have examined the consolidated balance sheet of Stancor Limited and subsidiary companies as at December 31, 1967 and the consolidated statements of profit and loss, deficit and source and application of funds for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the companies as at December 31, 1967 and the results of their operations and the source and application of their funds for the year then ended, in accordance with generally accepted accounting principles which, except for the change in the basis of amortizing deferred start-up and re-organization costs as described in note 5, have been applied on a basis consistent with that of the preceding year.

Clarkson, Gordon & Co.,
Soberman, Isenbaum & Nisker,
Chartered Accountants.

Toronto, Canada,
March 8, 1968.

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CONSOLIDATED BALANC

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CONSOLIDATED PRO-FORMA BALANCE SHEET AFTER

DECEMBER 3

ASSETS

	Actual	Pro Forma
CURRENT ASSETS:		
Accounts receivable	$2,239,829	$2,239,829
Inventories	2,023,692	2,023,692
Prepaid expenses and other current assets	37,220	37,220
Total current assets	4,300,741	4,300,741
PROPERTY, PLANT AND EQUIPMENT	3,397,774	3,397,774
GOODWILL - at cost	2,805,727	2,805,727
	$10,504,242	$10,504,242

NOTES:

1. This Balance Sheet has been prepared from the audited Consolida report of Stancor Limited. The notes to the audited financial with this Balance Sheet.
2. The Consolidated Pro-Forma Balance Sheet reflects the financial after giving effect to the Plan of Reorganization approved by t
3. Under the terms of the Plan of Reorganization approved June 28, Convertible Collateral Trust Debentures will be exchanged for c above does not include an amount of $30,139 to be exchanged for May 15, 1968.
4. Since December 31, 1967, 95,750 common shares have been issued of $957.50. This has reduced the price at which General Mortga Purchase Warrants may be converted into Common Shares from $8.0

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ANCE SHEET (NOTE 1)

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ER GIVING EFFECT TO REORGANIZATION (NOTE 2)

R 31, 1967

LIABILITIES

	Actual	Pro Forma
CURRENT LIABILITIES:		
Bank indebtedness	$2,766,452	$2,660,403
Accounts payable and accrued charges	1,255,421	1,176,806
Sales and other taxes payable	154,402	154,402
Long-term debt principal and interest payments due but unpaid	260,267	
Long-term debt principal due within one year	177,000	
Total current liabilities	4,613,542	3,991,611
NON-CURRENT LIABILITIES:		
Long-term debt (note 4)	3,928,295	4,499,115
Less unamortized debt discount and expense	194,428	194,428
	3,733,867	4,304,687
SHAREHOLDERS' EQUITY:		
Capital stock (notes 3 and 4)	3,713,800	3,764,911
Contributed surplus	8,500	8,500
(Deficit) earned surplus	(1,565,467)	(1,565,467)
	2,156,833	2,207,944
	$10,504,242	$10,504,242

dated Balance Sheet, dated December 31, 1967, included in the 1967 annual
l statements, which are an integral part thereof, have not been republished

al position of the Company as it would have appeared at December 31, 1967,
the Board of Directors June 28, 1968.
8, 1968, interest payable November 15, 1967 and May 15, 1968 on the
common share capital of the Company. The pro-forma Capital Stock shown
or the interest payable in respect of the period January 1, 1968 to

d under a trust arrangement for employees of the Company for a consideration
gage Debentures, Collateral Trust Debentures, Preference Shares, and Share
.00 to $6.22 per Common Share.

STANCOR LIMITED

Whitby, Ontario · Canada · 416/668-3315

July 8, 1968

TO THE SHAREHOLDERS:

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Because of a soft market for home furnishings during much of 1967, the Sklar and Peppler-Selig Divisions managed only to break even on operations in the first half. It was, therefore, impossible for the Company to absorb the Peppler loss. By May of 1967, the ability of the Company to pay its trade suppliers had deteriorated badly, and the bank had refused to increase its line of credit. It was obvious that drastic action had to be taken if the Company was to be saved.

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Yours very truly,

STANCOR LIMITED,

Samuel Sklar

Samuel Sklar,
President.